FILE COPY

IN THE

Supreme Court of the United States

OCTOBER TERM, 1948

Nos. 498 - 499

AMERICAN LOCOMOTIVE COMPANY

Petitioner

vs.

CHEMICAL RESEARCH CORPORATION

Respondent

AMERICAN LOCOMOTIVE COMPANY

Petitioner

vs.

GYRO PROCESS COMPANY

Respondent

PETITION AND BRIEF OF AMERICAN LOCOMOTIVE COMPANY FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

ANGELL, TURNER, DYER & MEEK
2103 Dime Building
Detroit 26, Michigan
Attorneys for Petitioner

CHARLES H. TUTTLE
C. DICKERMAN WILLIAMS
THEODORE L. HARRISON
TYLER M. BARTOW
WALTER M. MEEK
of Counsel

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PETITION OF AMERICAN LOCOMOTIVE COMPANY FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

TO THE HONORABLE, THE CHIEF JUSTICE OF THE UNITED STATES AND THE ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

The petition of the defendant American Locomotive Company respectfully shows:

Petitioner seeks review of a decision by the United States Court of Appeals for the Sixth Circuit, filed De-

cember 8, 1948, affirming the denial by Judge Picard, holding the United States District Court for the Eastern District of Michigan, Southern Division, of the petitioner's applications in these actions for stays under Section 3 of the United States Arbitration Act (R. 402, 458, 508). That Court's opinion is not yet reported. It is printed in the Record at pages 508-518. Judge Picard filed no formal opinion.

The petitioner's right to arbitration is based on paragraphs 4 and 9 of the contract with Gyro Process Company, dated June 16, 1932. On that contract these suits are brought, and to it the petitioner, as successor in interest to Alco Products, Inc. and as its guarantor, was a party (R. 216, 225). The other defendants are certain of its officers and directors, and are not parties to this proceeding.

These suits were instituted in 1940 and were consolidated by order entered March 1, 1946 (R. ix). Both claim breaches by the petitioner of the 1932 contract to which, by endorsement at the end thereof, Chemical Research Corporation as majority stockholder of Gyro Process Company (the other plaintiff), became a party both beneficiary and obligated (R. 224). The Pure Oil Company, minority stockholder in Gyro Process Company, sold its stock to Gyro in December, 1939, and then ceased to have any interest in the contract (R. 414).

Gyro's suit is the principal suit. The questions discussed in this petition are common to both.

Summary and Short Statement of Matter Involved

This petition and the decision of the Court of Appeals involve the construction and application of Section 3 of the United States Arbitration Act (9 U. S. C. A.) which reads:

> "Sec. 3. That if any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, *providing the applicant for the stay is not in default in proceeding with such arbitration.*" (Italics ours.)

The Court of Appeals, in its opinion, decided:

1. The petitioner had not, by its letter of September 27, 1938, "cancelled the provisions thereof (the contract) providing for arbitration", or "lost any arbitration rights provided by the contract" (R. 514).

2. "The controversy falls within the arbitration provisions" (R. 515-16).

3. Whether petitioner's interposition of a counterclaim, in the Gyro suit "constituted a technical waiver by Locomotive of its contract right of arbitration", was expressly left undecided (R. 516).

4. The petitioner was "in default" within the meaning of the proviso in Section 3 of the Arbitration Act, and hence could not have a "stay" under that Section (R. 517-18).

5. This application of the words "in default" in Section 3 was made not as "a matter of discretion", but as a matter of "judgment" (R. 518).

In thus holding that the petitioner was "in default" within the meaning of Section 3, the Court of Appeals frankly acknowledged its creation of *a judicial conflict*, saying (R. 518):

> "In doing so we give the word a broader meaning than is attributed to it in *Kulukundis Shipping Co.* v. *Amtorg Trading Corp. supra*, at page 989."

The decision thus referred to as not followed was by the Circuit Court of Appeals for the Second Circuit, reported in 126 Fed. (2d) 978, 989, and was reaffirmed by that Court in *Almacenes Fernandez, S. A.* v. *Golodetz*, 148 Fed. (2d) 625 (C. C. A. 2). We shall further show that the decision below was *also* in conflict with *Shanferoke* v. *Westchester Co.*, 293 U. S. 449. These basic *conflicts* will be analyzed in Points I and II, *post*.

The Court of Appeals below also held (R. 516-17):

> "Although Locomotive pleaded its contract right of arbitration, it was pleaded as a bar to the action with no reference to the provisions of the Arbitration Act. Under the Act, arbitration is not a bar, and in order to obtain the benefits of the provisions of § 3 thereof further action is necessary."

This statement refers to the fact that in its Answers in both suits, filed respectively in February, 1941, and November, 1942, the petitioner had pleaded as an affirmative "Defense" that under the contract of 1932 the controversy (R. 42, 424):

"should be heard and determined only by arbitration, as in said contract more specifically set forth; that no such arbitration has been had or demanded by said Gyro Process Company, plaintiff herein, and that plaintiff accordingly is not entitled to bring this action."

We shall show in Point II, *post*, that this Supreme Court and other courts have held that such an affirmative defense negates "default" within the meaning of the proviso in Section 3.

The petitioner respectfully challenges these rulings of law by the Court below as to the meaning of the statutory words "in default" and as to the irrelevance of the said affirmative Defense. The petitioner also challenges the Court's application of these rulings to the facts of the case.

Jurisdiction

The jurisdiction of this Court is invoked under Title 28, Section 1254, of the United States Code.

The Statute Involved

The statute involved is the United States Arbitration Act (9 U. S. C. A.), a copy of the relevant sections of which is printed in the Appendix.

Brief Statement of the Facts

1. The suit of Gyro Process Company was begun on August 30, 1940, by a complaint which occupies fifteen pages of the Record, contained four Counts and asked as damages $5,250,000 (R. 1-15).

2. The suit by Chemical Research Corporation was begun on June 19, 1940, by a complaint which occupies six pages of the Record. It contained two Counts and asked as damages $5,000,000 (R. 409-15).

To both suits the petitioner promptly filed answers containing denials and affirmative defenses, including the aforesaid affirmative Defense that under the contract the controversy "should be heard and determined only by arbitration" (R. 42, 424). The answers contained counterclaims which, in its brief below, the petitioner expressly offered to have included in the arbitration. Both suits were consolidated on March 1, 1946 (R. ix).

3. In November 1940, and before the petitioner had answered Gyro's original complaint, Gyro asked for discovery "to enable it to elaborate and complete its Declaration" (R. 25-6).

Thereafter, and down to March 17, 1941, it procured a series of orders extending its time thus to amend and "to elaborate and complete its Declaration" until twenty (20) days after the conclusion of its discovery, and "staying all proceedings in the above case, except the taking of certain depositions and testimony on discovery" (R. 32, 72, 77, 80).

After an initial discovery session in early 1941, Gyro *suspended the discovery for five years* (R. 358-9) and did not resume it until September 1946 (R. 511). On February 25, 1946, Gyro had changed attorneys (R. 156).

4. On September 6, 1946, Gyro's new attorney stated, as his position, that the discovery related not only to issues already in the case but also

"to issues which may at some time after this date be injected into the case by amendments" (R. 361-2).

As late as November 6, 1947, Gyro's attorney said (R. 363):

> "We are trying to find out the facts so we can prepare a complaint that will be *a comprehensive, accurate complaint.*" (Italics ours.)

At last, on December 19, 1947, Gyro filed a so-called "Amended and Supplemental Complaint" which increased the number of Counts from four to six, increased the number of pages from fifteen to one hundred thirty-nine, and increased the damages asked from $5,250,000 to $36,285,000 (R. 158-296). It presented immense areas of new subject-matters, claims and issues,—some of them arising during *the seven years* since the starting of the suit by the original complaint (R. 163, 173, 181, 186, 200, 202, 210). Hence, the descriptive word "Supplemental" (R. 158). Counts III, IV, V and VI in the new complaint, totalling $36,000,000 in damages, were notably different from anything in the original complaint. Count IV in the original complaint was dropped. See Point II, subd. 2, *post*.

This new complaint was not a mere amendment of the original complaint. It was a complete substitution and supersession. It covered seven additional years. Hence, it was the practical equivalent of starting *a new suit*. See Point II, *post*.

In short, Gyro had for its own advantage kept the case for seven years *in the pleading stage*.

5. Thereafter, and before the defendants' time "to file their response" to this superseding Amended and

Supplemental Complaint had expired (R. x and 157; and Rule 12), *and hence before issue was joined,* the petitioner applied under Section 3 of the United States Arbitration Act for a stay pending arbitration (R. 299). Its moving papers alleged (R. 301):

> "5. American Locomotive Company is now, and has at all times been, ready, willing and desirous of having all the issues involved in this action submitted to arbitration pursuant to the terms of the 1932 contract, but no such arbitration has been had or requested by the plaintiff or by Chemical Research Corporation."

Questions Presented

1. What, in view of the judicial conflict acknowledged to be created by the decision below, is the true interpretation and application of the words "in default" in the proviso in Section 3 of the Arbitration Act? See Point I, *post.*

2. In view of the conflict between the decision below and the decisions of this Supreme Court and other courts as to the relevance and effect under Section 3 of an affirmative defense pleading the right to arbitration, what is *now* the law on this important subject? See Points II and III, *post.*

3. Can a defendant, who immediately pleads the agreement to arbitrate as an affirmative defense to the original complaint, be held "in default" under the proviso of Section 3 when he promptly applies for "a stay" within his time to respond under Rules 12 and 15(a) to a super-

seding "Amended and Supplemental Complaint"? See Point III, *post*.

4. Can a defendant who so pleads to the original complaint, and who is then confronted by the plaintiff with discovery proceedings and a stay for the avowed purpose of substituting a superseding complaint with new issues and additional claims and subject matters, be held to be "in default" under Section 3 if he applies thereunder for a stay while the case is still in the pleading stage under Rule 12? See Point III, *post*.

5. Is the Court's decision that Section 3 may not be effectively utilized at a time when the petitioner was still entitled, under Rule 12 of the Rules of Civil Procedure, to move, object, respond, and plead defenses, claims and cross-claims, whether equitable or otherwise, reconcilable with the Act itself, with Rule 12, and with the decisions in the *Shanferoke* case, 293 U. S. 449, and other cases which we will cite in the ensuing brief? See Points II and III, *post*.

6. Is the Court's restrictive concept of the scope and role of arbitration under the Arbitration Act sustainable in view of the contrary and wider concept in prior decisions by the Supreme Court and other courts, and made manifest by the text, history and purpose of the Act itself?

Reasons Relied On for the Allowance of the Writ

1. The Court below has expressly acknowledged its conflict with the Circuit Court of Appeals for the Second Circuit in the *ratio decidendi*, to-wit, its interpretation and application of the words "in default" in the proviso in Section 3.

2. As we shall show in the ensuing brief, its interpretation and application are also in conflict with decisions by the United States Supreme Court and by other courts.

3. The question whether covenants for arbitration are pleadable and effective (to quote this Court in the *Shanferoke* case, 293 U. S. 449, 452) as "an equitable defense or cross-bill" *under the Arbitration Act*, is a question of law of general importance and of vital concern to the business community, the administration of jurisprudence and the whole public policy as to arbitration.

4. The policy of settling disputes by arbitration, and the reflection of that policy in the broad and comprehensive sanctions in the United States Arbitration Act, are of vital and constantly increasing importance to the economy and jurisprudence of the nation.

Hence, a restriction on its use and availability by a judicial interpretation broadening the operation of *the proviso clause*, urgently calls for review by the court of last resort,—particularly where such interpretation is the subject of acknowledged judicial conflict.

WHEREFORE, petitioner respectfully prays that a writ of certiorari be issued out of and under the seal of this

Honorable Court directed to the United States Court of Appeals for the Sixth Circuit, commanding that Court to certify and to send to this Court for review and determination, on a day certain to be therein named, a certified transcript of the record and proceedings herein; and that the petitioner may have such other and further relief in the premises as to this Honorable Court may seem meet and just.

Dated, January 4, 1949.

Respectfully submitted,

AMERICAN LOCOMOTIVE COMPANY,
Petitioner,

By CHARLES H. TUTTLE,
C. DICKERMAN WILLIAMS,
THEODORE L. HARRISON,
TYLER M. BARTOW,
WALTER M. MEEK,
Of Counsel.

ANGELL, TURNER, DYER & MEEK,
2103 Dime Building,
Detroit 26, Michigan,
Attorneys for Petitioner.

BRIEF

POINT I

The interpretation by the Court below of the words "in default" in Section 3 of the United States Arbitration Act is in admitted conflict with that of the Circuit Court of Appeals for the Second Circuit in the *Kulukundis* case.

It is also, we submit, in conflict with the decisions of the Second Circuit and of this Court in the *Shanferoke* case, and with the decision of the Second Circuit in the *Almacenes* case.

Moreover, it is in conflict with the plain meaning of the word "default" in Section 4 of the same Act.

1. As already stated, the Court below admitted that its result was arrived at by adopting "a broader meaning than is attributed to it (the word 'default' in Section 3) in *Kulukundis Shipping Co.* v. *Amtorg Trading Corp.*, supra, at page 989" (R. 518).

In reality, this admission was an understatement, for the Second Circuit in the *Kulukundis* case refused to regard even "delay" as relevant, much less equivalent, to "default", and construed the word "default" in the proviso as applying to an entirely different situation.

In the *Kulukundis* case (126 Fed. [2d] 978), the answer to the libel did not refer to arbitration but, on the contrary, by affirmative defenses denied both the alleged charter party and jurisdiction in admiralty. The libelee then propounded certain interrogatories; and, nearly a year after the libelant had responded thereto and five

months after the case had been marked ready for trial, the libelee moved for leave to amend its answer by setting up as an affirmative defense that the charter party (which it had denied and continued to deny) contained a provision for arbitration which the libelant had not invoked before suing. (See Record on Appeal therein.) The District Court denied the motion to amend; but the Circuit Court of Appeals for the Second Circuit reversed and held that the motion to amend should have been granted, and that, if the facts stated in the proposed affirmative defense were established, the District Court should, by granting a stay, require the case to go to arbitration. The Circuit Court of Appeals said (p. 989):

> "There remains to be considered the language of Section 3 of the Act, that 'on application,' such a stay shall be granted 'providing the applicant for the stay is not in default in proceeding with such arbitration.' We take that proviso to refer to a party who, when requested, has refused to go to arbitration or who has refused to proceed with the hearing before the arbitrators once it has commenced. The appellant was never asked by appellee to proceed with the arbitration; indeed, it is the appellee who has objected to it."

The Second Circuit then proceeded to discuss its earlier and like interpretation of the same proviso in the *Shanferoke* case, pointing out that its decision in that case had been affirmed by the Supreme Court. In the *Shanferoke* case the defendant had pleaded as "a special defense" precisely what the petitioner here had pleaded (R. 42), to-wit, the arbitration covenant and its willingness to arbitrate. The Second Circuit had upheld the efficacy of this affirmative defense and granted a stay under Section 3. It said at 70 Fed. (2d) 297, 299:

"The plaintiff further objects that the defendant is 'in default in proceeding with such arbitration,' within the meaning of section 3. True, it has not named its arbitrator, but in its answer and moving affidavits has merely expressed its willingness to submit to arbitration. This appears to us enough. It was the plaintiff who declared the contract to be at an end; and with that the defendant was contented. If the plaintiff meant to proceed further and enforce a claim for damages, the initiative rested upon it; it should have named the first arbitrator. *If it did not but sued instead, it was itself the party who fell 'in default in proceeding with such arbitration,' not the defendant.*" (Italics ours.)

This interpretation and application of Section 3 and of the efficacy of just such an affirmative defense as was pleaded in the instant case, was expressly adopted and affirmed by the Supreme Court on the appeal in the *Shanferoke* case (293 U. S. 449). To quote (p. 453):

"*Third.* The plaintiff also contends that the defendant was not entitled to a stay * * * because, on the facts developed by the affidavits, the defendant appears to have waived its rights under the arbitration clause by unreasonable delay in demanding arbitration. The reasons why these contentions are without merit are sufficiently stated in the opinion of the Court of Appeals."

The decision of the Second Circuit in the *Kulukundis* case was reaffirmed by it in *Almacenes Fernandez, S.A.* v. *Golodetz*, 148 Fed. (2d) 625, 627-8 (C. C. A. 2) where a stay under Section 3 was granted notwithstanding that the defendant had pleaded affirmative defenses and a counterclaim and had moved to bring in seven third party defendants, and notwithstanding that about six months

elapsed before it moved for a stay. See discussion of and quotation from this decision in Point II, *post.*

2. The Second Circuit's interpretation of "default" in Section 3 is also clearly confirmed by Section 4 wherein that word repeatedly occurs.

Section 4 reads:

> "A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any court of the United States which, save for such agreement, would have jurisdiction under the judicial code at law, in equity, or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner provided for in such agreement. Five days' notice in writing of such application shall be served *upon the party in default.* * * * If no jury trial be demanded *by the party alleged to be in default,* or if the matter in dispute is within admiralty jurisdiction, the court shall hear and determine such issue. Where such an issue is raised, *the party alleged to be in default* may, except in cases of admiralty, on or before the return day of the notice of application, demand a jury trial of such issue, and upon such demand the court shall make an order referring the issue or issues to a jury in the manner provided by law for referring to a jury issues in an equity action, or may specially call a jury for that purpose. If the jury find that no agreement in writing for arbitration was made or *that there is no default in proceeding thereunder,* the proceeding shall be dismissed. If the jury find that an agreement for arbitration was made in writing and *that there is a default in proceeding thereunder,* the court shall make an order

summarily directing the parties to proceed with the arbitration in accordance with the terms thereof." (Italics ours.)

The purpose of the proviso at the end of Section 3 is to prevent a contracting party from blocking *both* the judicial and the arbitrational methods of determining controversies with the other party. He may not hold the judicial method in suspense if he is already, by refusing to proceed with arbitration, holding the arbitrational method in suspense. Section 4 shows that one who is holding the arbitrational method in suspense by refusing to cooperate in determination by arbitration, is regarded as being "in default" within the meaning of that Section. The two Sections, read together, prevent a litigant from effectively blocking a determination by either method of trial, or from blocking either method of securing arbitration.

POINT II

Moreover, for seven years Gyro avowedly kept the case in the pleading stage, for the express purpose of an ultimate superseding complaint.

Nevertheless, the petitioner immediately pleaded its right to arbitration; and, when the superseding "Amended and Supplemental Complaint" was filed, the petitioner immediately responded within the time allowed by Rules 12 and 15(a) by an application for a stay under Section 3.

Hence that application was a proper and timely response under Rules 12 and 15(a) and was also a proper and timely "equitable defense and cross-bill" under *Shanferoke* v. *Westchester Co.*, 293 U. S. 449, 452.

The holding below that petitioner was "in default" conflicts with both the Rules and the decisions, and confines the stage of pleading to "a one-way street" for Gyro's benefit. Gyro could at its leisure substitute an Amended and Supplemental Complaint, but the petitioner could not exercise the full right of response thereto given it by Rules 12 and 15(a) and by the procedures of law applicable to the pleading stage.

(1) This Court has specifically held that such a motion under Section 3 is in the nature of "an equitable defense or cross-bill" (*Shanferoke* v. *Westchester Co.*, 293 U. S. 449, 452).

In *Murray Oil Products Co.* v. *Mitsui & Co.*, 146 Fed. (2d) 381 (C. C. A. 2), the Second Circuit held that Section 3 "modifies the procedure *only* by substituting arbi-

tration as the mode of trial", and neither bars nor is barred by "the usual provisional remedies" in the action (p. 384).

(2) As set forth in the foregoing petition, Gyro procured at the very outset sweeping orders for discovery and general stay, sought and granted for the very purpose of enabling it "to elaborate and complete its Declaration" (R. 77), and to enable it to inject new "issues into the case by amendments" (R. 361-2, 481-2). Thus Gyro for its own advantage kept the case in the pleading stage.

Ultimately, Gyro filed its "Amended and Supplemental Complaint" on December 19, 1947 (R. 158).

As already stated, this new pleading was *a complete substitution and supersession*. In comparison with the original Complaint, it increased the Counts from four to six, the number of pages from 15 to 139, and the damages from $5,250,000 to $36,285,000 (R. 158-296). It also greatly extended the periods of time involved. Instead of speaking solely as of August 30, 1940,—the date of the original Complaint (R. 1),—it covered the intervening period from that date to the date of the filing of the superseding Complaint on December 19, 1947 (R. 158). Thus, in paragraph 14 (adapted and repeated in connection with each of the Counts, R. 173, 181, 186, 200, 202, 210), it referred to acts and conduct of the defendant since June 16, 1932, not only "up to and including the date of the commencement of this suit" but "also to the date of filing of this Amended and Supplemental Complaint" (R. 167)—*an additional period of over seven years after the commencement of the suit*. Hence, the descriptive term "Supplemental" was an accurate characterization of new and imposing claims.

As a matter of practical reality this new superseding pleading was the commencement of a new suit.

Thus, Gyro itself had purposely kept the case continuously *in the pleading stage* from November, 1940. Hence, when on December 19, 1947, it filed a superseding complaint with supplemental charges covering the whole fifteen years from the making of the contract to that date, it automatically extended the stage and scope of response as authorized in Rules 12 and 15(a) and automatically endowed the petitioner with all the various rights granted by those two Rules and by the procedures of law applicable to the pleading stage. It was not confined to any of the responses it had made to the original complaint.

As the Sixth Circuit said in another case, *Grubbs* v. *Smith*, 86 Fed. (2d) 275 (certiorari denied, 300 U. S. 658):

> "But whatever the plaintiff's intention, as a matter of law the amended and substituted petition superseded the prior pleadings in the case."

In *Almacenes Fernandez, S. A.* v. *Golodetz,* 148 Fed. (2d) 625 (C. C. A. 2), the Second Circuit cited with approval the holding in *Short* v. *National Sport Fashions, Inc.*, 264 App. Div. (N. Y.) 284, that a demand for arbitration made *after* the service of an amended pleading and before the time to respond thereto had expired, was timely, because *"the action at law was still in the pleading stage"* (p. 285).

(3) To deny the petitioner the right of responding with a Section 3 application at a time when it could have responded with any other motion, objection, defense, claim

or cross-claim, legal or equitable, wholly violates Rules 12 and 15(a) and also this Court's concept of such an application as "an equitable defense or cross-bill" as declared in the *Shanferoke* case (293 U. S. 449, 452).

In that case this Court, holding that the denial of a petition for a stay of trial under Section 3 was appealable under former Section 129 of the Judicial Code, said that such a petition was "an equitable defense or cross-bill" (p. 452).

In so holding, this Court adopted its discussion of equitable defense and cross-bill in *Enelow* v. *New York Life Insurance Co.*, 293 U. S. 379, decided the same day. In the *Enelow* case this Court, discussing Section 274b, said that (p. 382):

> "Equitable defenses were permitted (by § 274b) to be interposed in actions at law 'by answer, plea or replication without the necessity of filing a bill on the equity side of the court.' *The defendant is to have 'the same rights' as if he had filed a bill seeking the same relief.*" (Italics ours.)

An equitable cross-bill may be brought at any time. In the *Enelow* case this Court at page 383 cited *Ford* v. *Huff*, 296 Fed. 652, and *American Cyanamid Co.* v. *Wilson & Toomer Co.*, 62 Fed. (2d) 1018, cert. den. 289 U. S. 735, both decisions of the Court of Appeals of the Fifth Circuit.

In *Ford* v. *Huff*, *supra*, the Circuit Court of Appeals sustained an equitable plea filed a number of months after the joinder of issue in an action at law. The District Court said that "such plea can be offered at any stage of the proceedings before the trial is actually had" (289 Fed. 858, 869). In consequence, the Court of Appeals sus-

tained the plea on the merits, and held its filing to be timely on the very ground that "at the time" an amended pleading was "proper" (296 Fed. 654). See also Rule 15(a).

In the later *American Cyanamid* case, *supra,* 62 Fed. (2d) 1018, an equitable plea was filed in an action at law *after two trials* of that action. The same Court of Appeals held the plea timely, saying at page 1020:

> "Nor do we think the fact that the plea was first presented to the court on the very eve of trial at law and after there had been previous trials prevents its due consideration. Under the old practice proceedings at law could be enjoined by a defendant in order to assert a good equitable defense at any stage, either to stay trial, to stay execution, or sometimes to stay the money in the sheriff's hand or his execution of a writ of possession. *Burnes* v. *Scott,* 117 U. S. at page 588."

In the *Enelow* case (293 U. S. 379) this Court specifically cited with approval (p. 383) this page 1020 of the opinion in the *American Cyanamid* case.

(4) Moreover, an application under Section 3 for a stay pending remission of the issues for trial by arbitration bears an analogy to an application for remission of the issues (whether in a jury case or otherwise) to a special master for an advisory opinion.

This analogy was drawn by the Circuit Court of Appeals for the Second Circuit in the *Mitsui* case, 146 Fed. (2d) 381, 383:

> "Arbitration is merely a form of trial, to be adopted in the action itself, in place of the trial at common law: it is like a reference to a master, or an 'advisory trial' under Federal Rules of Civil Procedure, Rule

39(c), 28 U. S. C. A. following section 723c. That is the whole effect of § 3."

Such an application for a special master, with accompanying request for a stay, cannot be made under the rules of law until *after* issue is finally joined.

Rules 16 and 53 of the Rules of Civil Procedure;
53 *C. J.* 695-6;
21 *C. J.* 606;
Michelson v. *Shell Union Oil Corp.*, 1 F. R. D. (Mass.) 183, 184.

A fortiori, an application under Section 3 for a stay pending the agreed mode of trial before a board of arbitrators cannot in law be condemned as "in default" in a case where the original complaint has been completely superseded, issue thereon has not yet been joined, and the defendant's time under Rule 12 to present as of right motions, objections, defenses and pleadings has not expired but has been thrown wide open by the plaintiff itself.

POINT III

Furthermore, in holding the petitioner "in default" under Section 3, by reason of submitting to Gyro's unappealable orders for discovery and for a stay pending the superseding of Gyro's original complaint, the Court below is in conflict with the decisions of this Court and of the Second Circuit that the usual provisional remedies are available under Section 3 and do not outlaw the right to move for a stay thereunder,—particularly where, as here, the defendant had promptly pleaded as an affirmative defense its right to arbitration.

The Arbitration Act "modifies the procedure only by substituting arbitration as the mode of trial."

1. Section 3 of the Arbitration Act provides only for a stay of *"the trial of the action."*

There is nothing in Section 3 limiting the rights of the parties to conduct interlocutory proceedings for the purpose of obtaining discovery of evidence for a new pleading or even for trial. On the contrary, those rights, as both this Court and the Second Circuit have unequivocally declared, continue to exist without impairment by that Section. The exercise of them or the submission to them does not constitute a "default" within the meaning of the proviso in Section 3.

Moreover, promptly after the start of the suit, the petitioner had pleaded as an affirmative defense its right to arbitration (R. 42), and Gyro knew that that defense was part of the pleading stage which Gyro was keeping open for a new complaint by it.

In *Murray Oil Products Co.* v. *Mitsui & Co.*, 146 Fed. (2d) 381 (C. C. A. 2), the Second Circuit gave an extended and most informative discussion of the interrelationship between court actions and arbitration with special reference to Section 3. The Circuit Court said, at p. 384:

> "It was implictly assumed (by Congress) that actions brought under § 3 would proceed throughout in accordance with the practice, applicable to them if arbitration were not the method of trial."

The Circuit Court also said, at p. 384:

> *"We think an arbitration clause does not deprive a promisee of the usual provisional remedies, even when he agrees that the dispute is arbitrable.*
>
> "As we have seen, § 3 allows such actions to be brought upon contracts containing such clauses, and *modifies the procedure only by substituting arbitration as the mode of trial.* The promisee retains all those remedies after judgment that he has in any other action; * * * All these things considered, we cannot think that we should import into the section a limitation (on interlocutory proceedings), which language does not demand, which could operate over only part of the field (i.e., before judgment), and which, so far as we can see, would be as likely to defeat as to aid the purpose of the act." (Italics ours.)

In *The Anaconda* v. *American Sugar Co.*, 322 U. S. 42, the Supreme Court said of Section 3 (p. 44):

> "The section obviously envisages action in a court on a cause of action and does not oust the court's jurisdiction of the action, though the parties have agreed to arbitrate. And, it would seem there is nothing to prevent the plaintiff from commencing

the action by attachment if such procedure is available under the applicable law."

In *Almacenes Fernandez, S. A.* v. *Golodetz,* 148 Fed. (2d) 625 (C. C. A. 2) the Circuit Court squarely held that various interlocutory proceedings by the defendant in the case did not bar it from applying for a stay under Section 3. The Circuit Court said (pp. 628-9):

> "The first (argument against the stay) is that the right to insist upon arbitration was waived by Golodetz & Co. when it answered the complaint with affirmative defenses and a counterclaim and when it invoked the jurisdiction of the district court to bring in third party defendants. * * * Such action did not indicate an intention on the part of Golodetz & Co. to abandon its right to insist on arbitration, which it had already alleged as a defense, and so fell short of a waiver of it."

These decisions fit this case like a glove and squarely conflict with the decision below.

In *Matter of Haupt & Co.* v. *Rose,* 265 N. Y. 108, the defendant had secured an order requiring plaintiff to state separately and number its causes of action, and plaintiff thereafter served an amended complaint accordingly. When the plaintiff argued that defendant had thereby waived its right of arbitration, the Court of Appeals held that the defendant was not required to choose until the amended complaint had been served. It said (p. 111):

> "When Rose served his complaint, Haupt & Co. was entitled * * * to have it framed as required by law before an imperative duty arose to make an election (as between court trial and arbitration) * * *. Here Haupt & Co., following the service of the

amended complaint, moved promptly and before its time to answer expired. The only election made by Haupt & Co. was to proceed by arbitration."

In *Matter of Catino Contracting Co.* v. *Gelson Realty Corp.*, 173 Misc. 239 (Sup. Ct. Bronx Co.), the Court said (pp. 241-2):

"None of the other steps taken by the petitioner in the City Court action, namely, its demand for a bill of particulars, its motion to preclude for failure of respondent to serve a bill of particulars, nor the making of a motion for judgment on the pleadings, constituted a waiver. These were all steps taken in an action in which the petitioner had pleaded the arbitration clause in the contract as an indication of an intent not to waive his rights under it."

2. All these decisions are in complete disagreement with the law as declared in the decision below.

They all hold that the institution of interlocutory proceedings or submission to them while the case is still in the pleading stage and before issue is finally joined, is neither a bar to nor a waiver of the right to enforce arbitration,—particularly where, as in this very case, the defendant had answered the original complaint with an affirmative defense based on the arbitration covenant itself (R. 42).

Under those decisions the test lies in the adopted mode of trial, not [illegible]here interlocutory proceedings looking to substituting new pleadings or gathering evidence.

The double error of the Court below lies, we respectfully submit, in interpreting the words "in default" as expressing the consequence of submission to such interlocutory proceedings and in then making that consequence

applicable as a permanent bar notwithstanding the coming of a superseding complaint equivalent in its character to the start of a new suit.

Both these errors inject serious restrictions and technical complexities into the broad policy of the United States Arbitration Act and should, we submit, be reviewed by the court of last resort.

3. Moreover, during this entire period the petitioner, so far from withdrawing or abandoning its affirmative defense based upon the arbitration covenants (R. 42), itself conducted interlocutory proceedings for the very purpose of establishing and fortifying that defense.

Thus, on May 27, 1942, the petitioner filed a "motion for deposition and discovery" "regarding any matter not privileged which is relevant to the subject matter involved in this pending action whether relating to the claim or defense of said petitioners or to the claim or defense of Gyro therein" (R. 96). The supporting affidavit expressly referred to the "separate defenses" as included in the objectives of the motion (R. 98, 100). The motion was granted in its entirety after an argument in which petitioner's counsel expressly asked for discovery "in connection with our special defense, *that they should first have resorted to arbitration*", and after the Court had indicated that a discovery for that very purpose was one "which I think they (the defendants) are entitled to" (R. 504-6).

Again, on January 29, 1946, two days before the expiration of the petitioner's time to answer Gyro's second (but not final) amended complaint, there was a hearing in court on petitioner's application for discovery of an enlarged and more specific list of Gyro's records. During that hearing the petitioner's counsel specifically rehearsed

the arbitration as what "we want" and asked discovery of all papers relative thereto (R. 487-9). The Court stated: "They (Gyro) will give you that" (R. 489); and thereupon included in its order for discovery by Gyro (R. 492):

> "(4) Any proposals or negotiations for *arbitration* under paragraphs 4 and 9 of Exhibit A attached to the plaintiff's second amended declaration." (Italics ours.)

Of course, in these hearings defense counsel spoke about the possibility of a "trial". Gyro had included in its discovery petition its intention to take issue on the affirmative defense as to arbitration (R. 78). Hence, a "trial" as to the applicability of that defense was always a consideration. Moreover, a "trial", whether by arbitrators or the Court, was inevitable.

4. In its opinion, the Court below made certain statements about "delay" which would be quite irrelevant if the Court had followed the foregoing decisions and had interpreted and applied the words "in default" in Section 3 in accordance with their true meaning,—and this quite irrespective of the world of difference between "delay" and "default".

Nevertheless, we wish briefly to comment on those statements as also, we respectfully submit, mistaken, fractional and inconsequential.

(a) The Court below states that Gyro might have "elected to handle the matter differently if the dispute was to be arbitrated" (R. 517).

This is pure speculation. The Record discloses no such claim, specification or proof by Gyro.

Moreover, the speculation is itself utterly refuted by Gyro's self-evident determination to accompany the very instituting of the suit itself with an eager and practically unlimited demand to search the petitioner's papers and examine its officers. Gyro had elected to sue and not to arbitrate. It had never offered to arbitrate. It followed its election with procuring an order freezing the case in the pleading stage while it prosecuted an unlimited fishing expedition in the petitioner's preserves. It chose to do so notwithstanding that it knew the petitioner's affirmative defense based on the right of arbitration.

Upon the argument of Gyro's petition on March 17, 1941, its then attorney, Mr. Groesbeck, said (R. 481):

> "At the time that this matter was up in December before your Honor, you gave very specific directions as to what should be done, and it was certainly our understanding of the matter that *all proceedings be stopped* until the order of the Court (for the discovery) was complied with. Now, we think that that ought to be followed." (Italics ours.)

(b) The Court below refers to the plaintiff's discovery proceedings as "expensive"(R. 517).

But these proceedings were begun by Gyro on November 25, 1940 (R. 22-7), even before the petitioner had filed its answer to the original complaint on February 8, 1941 (R. 33). The avowed purpose of the discovery was to enable Gyro to inject new subject matters, claims and issues and to file not only a superseding amended complaint but also a supplemental complaint (R. 361-3, 481-2). Ultimately Gryo did so use and climax its discovery.

An increase in claim from $5,250,000 to $36,285,000 leaves little room for sympathy over the matter of "expense".

(c) The Court below acknowledges "that Gyro can use in an arbitration proceeding the evidence it discovered through the discovery proceedings" (R. 517).

Hence, it certainly does not lie in the mouth of Gyro to claim that, because at its request the action was held in suspense and in the pleading stage until at its leisure it got set to file a superseding complaint, the petitioner thereby fell "in default" and forfeited, as regards the new pleading, a right expressly reserved to it by Rule 12.

(d) The Court below refers to "numerous agreed orders" during Gyro's discovery proceedings (R. 517).

But most of those orders were orders extending the petitioner's time to answer, and were made in view of Gyro's avowal that its preceding complaints were ultimately to be superseded by an altogether new complaint (R. 361-3). Indeed, the Court below, elsewhere in its opinion, expressly acknowledges that of these "agreed orders" "thirty-nine were entered extending the time (of Locomotive) to answer" (R. 510).

(e) The Court below states that "the discovery proceedings were started in May, 1941, but met objections from defendants, which required court rulings and clarifying orders" (R. 511).

There was only one court ruling, and that in June, 1941 (R. 358). After that ruling Gyro failed to "discover" for over five years (R. 358-9). Doubtless, this failure was due to a loss of interest in the action by Gyro's original attorneys, Messrs. Groesbeck & Sempliner (R.

66-7; 156; 489-90; 498-500). Mr. Van Auken was substituted on February 26, 1946 (R. 156). Obviously, if anybody was "in default", it was Gyro.

(f) The Court below, after referring to March 17, 1941, states that: "Numerous motions were thereafter actually made and passed upon" (R. 517).

But, actually, all such motions pertained to the discovery itself, except for the petitioner's motion to consolidate the Gyro and Chemical cases (R. v-ix).

(g) The Court below states that the petitioner "filed its motion for a stay on March 2, 1948, after a lapse of more than seven years" (R. 517).

We respectfully submit that this statement is scarcely fair, since it omits the facts that the plaintiff had waited for seven years to file its superseding complaint, and that petitioner had promptly moved for a stay under Section 3 before joinder of issue thereon and within its lawful time for any of the responses permitted by Rule 12.

(h) The Court below states that, after filing its answer in 1941, the petitioner made "no attempt" to proceed as to arbitration until it moved for a stay on March 22, 1948 (R. 517).

This is not accurate. Actually, in 1942 and again in 1946 the petitioner obtained orders against Gyro for discovery, for the very purpose of supporting its position "for arbitration under paragraphs 4 and 9 of the contract" (See Point III, subd. 3, *supra*).

POINT IV

The decision below is, we submit, also in flat contradiction of the fundamental principle of equity and justice that a party may not take advantage of or from his own default or delay.

Gyro was obligated to pursue arbitration. The 1932 contract expressly provided that disputes of the character specified in paragraphs 4 and 9 "shall be heard and determined *only* in the following manner", to wit, "arbitration" (R. 219, 221-2).

Instead Gyro sued and thereby it became itself the party "in default" (See *supra*, p. 15). Thereafter it delayed and froze the suit for seven years for the purpose of preparing a superseding complaint.

From the beginning Gyro was on notice that the petitioner had, by its answer, claimed *trial* by arbitration. It knew that the petitioner had secured orders for discovery in aid of its affirmative defense as to arbitration (Point III, subd. 3, *supra*).

Gyro now indulges in the irony of contending that, because for nearly seven years it never advanced the suit beyond the prospect of a new and superseding complaint by itself, the petitioner has lost the right to have "the trial" of Gyro's final allegations and ultimate claims conducted by arbitration as contracted.

Fundamental equitable principles, as well as the very terms and policy of the Arbitration Act, will not permit one contracting party to convert his own default, breach or delay into an advantage to himself and a forfeiture and penalty to the other party. To allow Gyro thus to capitalize on its own delinquency would be anomalous.

In *Modern Brokerage Corp.* v. *Massachusetts Bonding Co.*, 56 F. Supp. 696 (S. D. N. Y.), the Court characterized a similar contention at page 697 as

> "* * * a rather unusual objection which, if acquiesced in, would permit a party in an arbitration agreement to take advantage of his own default in order to relieve itself from a contractual obligation voluntarily assumed."

In *Spiller* v. *St. Louis & S. F. R. Co.*, 14 Fed. (2d) 284 (C. C. A. 8), there is the following statement of a familiar equitable principle (p. 288):

> "It is sound doctrine that, if a party interposing defenses of laches has been responsible for and substantially contributes to the delay, he is precluded from taking advantage thereof."

In *In re Indiana Concrete Pipe Co.*, 33 Fed. (2d) 594 (D. Ind.), a like principle is thus stated (p. 596):

> "Certainly a party cannot be charged with laches if the delay was induced by the party setting up the laches as a defense."

POINT V

Since the Court of Appeals disavowed deciding whether petitioner's inclusion of a counterclaim in its answer to Gyro's original complaint "constituted a technical waiver by Locomotive of its contract right of arbitration" (R. 516), we shall speak of the point only briefly.

1. It is impossible to see how inclusion in an answer of a counterclaim which expressly pleaded as an affirma-

tive defense the agreement for trial by arbitration (R. 42), could be a "waiver" of such a trial.

According to *Bennecke* v. *Connecticut Mutual Life Ins. Co.*, 105 U. S. 355, 359; and *Watkins* v. *Fly*, 136 Fed. (2d) 578, 580 (C. C. A. 5):

> "A waiver may be defined as the intentional relinquishment of a known right with both knowledge of its existence and an intention to reliquish it."

An intention to abandon a contractual right which is expressly asserted and relied on as a defense, is a contradiction in terms and in common sense.

Under Rule 13(a) and the principle of law which it embodies, the pleading of the counterclaim was "compulsory" since it arose out of the contract on which Gyro sued. Even if (contrary to the fact and the law) there was inconsistency between the defense and the counterclaim, nevertheless under Rule 8(e) of the Rules of Civil Procedure

> "a party may also state as many separate claims or defenses as he has regardless of consistency and whether based on legal or on equitable grounds or on both."

In *Kulukundis Shipping Co.* v. *Amtorg Trading Corp.*, 126 Fed. (2d) 978 (C. C. A. 2), the original answer to the libel denied the execution of the charter party. It said nothing about arbitration. Nine months later and about two months before the case was to be reached for trial, the libellee moved to amend its answer to *also* plead, as a separate defense, that the charter party contained an arbitration clause which the libellant breached by bringing the suit. The denial of the motion was reversed by the

Circuit Court of Appeals which held that such inconsistent positions could be taken in the libellee's answer (p. 988), and that the libellee was not guilty of a "waiver" and was not "in default" under Section 3 of the Arbitration Act.

Almacenes Fernandez, S. A. v. *Golodetz,* 148 Fed. (2d) 625 (C. C. A. 2), presented elements far more persuasive of waiver; and yet a stay under Section 3 of the Arbitration Act was affirmed. The Circuit Court of Appeals, in ruling against the plaintiff-appellant's arguments, said (pp. 627-8):

> "The first is that the right to insist upon arbitration was waived by Golodetz & Co. when it answered the complaint with affirmative defenses and a counterclaim and when it invoked the jurisdiction of the district court to bring in third party defendants. * * * Such action did not indicate an intention on the part of Golodetz & Co. to abandon its right to insist on arbitration, which it had already alleged as a defense, and so fell short of a waiver of it."

The Circuit Court of Appeals cited (p. 628) *Short* v. *National Sport Fashions, Inc.,* 264 App. Div. (N. Y.) 284, which held that the failure of the defendants to claim the right to arbitrate in their original answer did not constitute a "waiver" where they served an amended answer asserting that right, since *"the action at law was still in the pleading stage"* (p. 285).

2. Moreover, the Arbitration Act is concerned with "the trial", not with pleading. See Point III, *supra.* To quote again the *Mitsui* case, 146 Fed. (2d) 381, 384, the Arbitration Act "modifies the procedure only by substituting arbitration as the mode of trial".

3. In the present case, not only had Locomotive in its *original answer* promptly asserted the contractual right of arbitration and had thereafter conducted discovery proceedings for the establishment and enforcement of that affirmative defense (Point III, subd. 3, *supra*, and R. 96-100; 487-9, 492, 504-6), but at the very time when the petitioner moved for a stay the suit was, by election and action of Gyro itself, "still in the pleading stage" and the petitioner possessed all the rights given by Rule 12 to move, make objections, assert defenses, claims and cross-claims and to serve a responsive pleading.

CONCLUSION

The petition for a writ of certiorari, as prayed for, should be granted.

Dated, January 4, 1949.

Respectfully submitted,

CHARLES H. TUTTLE,
C. DICKERMAN WILLIAMS,
THEODORE L. HARRISON,
TYLER M. BARTOW,
WALTER M. MEEK,
Of Counsel for Petitioner.

ANGELL, TURNER, DYER & MEEK,
2103 Dime Building,
Detroit 26, Michigan,
Attorneys for Petitioner.

APPENDIX A

Section 2 to 6 (inclusive) of the United States Arbitration Act (Title 9, United States Code Annotated).

Section 2. "A written provision in any maritime transaction or a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract."

Section 3. "If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration."

Section 4. "A party aggrieved by the alleged failure, neglect, or refusal of another to arbitrate under a written agreement for arbitration may petition any court of the United States which, save for such agreement, would have jurisdiction under the judicial code at law, in equity, or in admiralty of the subject matter of a suit arising out of the controversy between the parties, for an order directing that such arbitration proceed in the manner pro-

vided for in such agreement. Five days' notice in writing of such application shall be served upon the party in default. * * * If no jury trial be demanded by the party alleged to be in default, or if the matter in dispute is within admiralty jurisdiction, the court shall hear and determine such issue. Where such an issue is raised, the party alleged to be in default may, except in cases of admiralty, on or before the return day of the notice of application, demand a jury trial of such issue, and upon such demand the court shall make an order referring the issue or issues to a jury in the manner provided by law for referring to a jury issues in an equity action, or may specially call a jury for that purpose. If the jury find that no agreement in writing for arbitration was made or that there is no default in proceeding thereunder, the proceeding shall be dismissed. If the jury find that an agreement for arbitration was made in writing and that there is a default in proceeding thereunder, the court shall make an order summarily directing the parties to proceed with the arbitration in accordance with the terms thereof."

Section 5. "If in the agreement provision be made for a method of naming or appointing an arbitrator or arbitrators or an umpire, such method shall be followed; but if no method be provided therein, or if a method be provided and any party thereto shall fail to avail himself of such method, or if for any other reason there shall be a lapse in the naming of an arbitrator or arbitrators or umpire, or in filling a vacancy, then upon the application of either party to the controversy the court shall designate and appoint an arbitrator or arbitrators or umpire, as the case may require, who shall act under the said agreement with the same force and effect as if he or they had been specifically named therein; and unless otherwise provided in the agreement the arbitration shall be by a single arbitrator."

Section 6. "Any application to the court hereunder shall be made and heard in the manner provided by law for the making and hearing of motions, except as otherwise herein expressly provided."